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PRAXAIR DISTRIBUTION INC.

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

FEDERAL INSURANCE COMPANY,

Plaintiff,

vs.

PRAXAIR DISTRIBUTION INC., a foreign corporation; HARSCO CORPORATION, SHERWOOD VALVE DIVISION, a foreign corporation; ad DOES 1 THROUGH 50, inclusive,

Defendants.

Case No. CV-04-03943 SC

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT PRAXAIR DISTRIBUTION, INC.'S MOTION FOR SUMMARY JUDGMENT OR, IN THE ALTERNATIVE, PARTIAL SUMMARY JUDGMENT

Hearing Date: Friday, September 2, 2005
Time: 10:00 A.M.
Place: Courtroom 1, 17th Floor

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Defendant Praxair Distribution, Inc. (hereinafter "PDI") submits the following Memorandum of Points and Authorities in Support of its Motion for Summary Judgment or, in the Alternative, Partial Summary Judgment pursuant to Rule 56 of the Federal Rules of Civil Procedure.

I. INTRODUCTION

Plaintiff Federal Insurance Company's (hereinafter "Federal") complaint alleges claims for negligence, strict product liability, and breach of warranty against defendants Praxair Distribution, Inc. and Harsco Corporation, Sherwood Valve Division. The subrogation complaint alleges a claim for damages arising from the alleged failure of the delivery and/or valve system of a cylindrical tank, model number 240 Plus, serial number 454-006-F6, which was to deliver liquid nitrogen into an automated biomedical holding chamber. The alleged failure purportedly caused the spoliation of biological matter on April 2, 2002 at the facility of plaintiff's insured, Exelixis, Inc. (hereinafter "Exelixis").

PDI and Exelixis' business relationship is governed by a contract that sets forth the terms of PDI's agreement to supply gas products to Exelixis. Because Federal succeeds under subrogation to the rights of its insured, Exelixis, Federal's right to sue PDI for damages under a negligence, strict liability, and breach of warranty theory is also governed and limited by the contract between PDI and Exelixis. The relevant contract contains both a limitation of liability provision and a limitation of damages clause. First, paragraph 8 of the contract provides: "No claim of any kind with respect to any of the Products delivered hereunder, whether based on contract, negligence, warranty, strict liability or otherwise, shall be greater than the price paid for the Products in respect to which such claim is made." Second, paragraph 9 of the contract provides: "Purchaser assumes all risk and liability for loss, damages or injury to persons or property arising out of the presence of or use of the Products. Seller will not be liable for any special, indirect, incidental or consequential damages hereunder, whether arising from failure to deliver the Products or negligence, warranty, strict liability or otherwise." Given these contractual limitations clauses, neither Exelixis nor Federal is entitled to maintain an action for damages against PDI as matter of law.

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PDI makes this motion for summary judgment on the sole issue of whether the terms of the contract extinguishes Federal's claims against PDI as a matter of law. Alternatively, PDI respectfully requests that the Court grant it partial summary judgment on the claims on which there are no genuine issue of material fact and on which PDI must prevail as a matter of law. PDI specifically reserves its right to move for summary judgment on other grounds, including causation, after further discovery.

II. STATEMENT OF FACTS

A. The Relationship Between PDI, Exelixis and Federal

PDI is a supplier of industrial, medical and specialty gases in cylinders and small cryogenic containers. Declaration of Bill Bright, ¶ 2. Exelixis is a pharmaceutical company engaged in the discovery and development of potential new drug therapies. Complaint, ¶ 7. Federal is an insurance company that issued a contract of insurance to Exelixis whereby Federal undertook to insure and indemnify Exelixis against certain business losses. Complaint, ¶ 8.

Federal alleges that PDI supplied Exelixis with a cylindrical tank, model number 240 Plus, serial number 454-006-F6, which failed to deliver liquid nitrogen into an automated biomedical holding chamber resulting in the spoliation of biological matter on or about April 2, 2002 at Exelixis' facility in South San Francisco. Complaint, ¶ 9. As a result of this alleged failure, Exelixis suffered a loss in the amount of $235,800, and Federal was obligated to pay a claim to Exelixis in the amount of $210,800 after Exelixis' deductible. Complaint, ¶¶ 18-19.[1]

PDI entered into a contract with Exelixis on April 18, 2000 to supply Exelixis with various gas products. Declaration of Bill Bright, ¶ 3, Exhibit 1. The contract was amended and renewed on December 4, 2000 and again on February 21, 2002. Declaration of Bill Bright, ¶¶ 4-5, Exhibits 2 and 3. The February 21, 2002 contract was the contract in effect at the time of the April 2, 2002 incident that is the subject of this action. Declaration of Bill Bright, ¶ 5, Exhibit 3.

[1] PDI does not concede that the facts alleged in Federal's complaint are true as discovery on the factual circumstances surrounding the incident continues. However, for purposes of this motion, PDI assumes Federal's allegations to be true and argues that PDI would still prevail as a matter of law even assuming Federal's allegations to be true.

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B. The February 21, 2002 Contract

The February 21, 2002 Contract between Exelixis and PDI (Declaration of Bill Bright, ¶ 5, Exhibit 3) provides several key terms governing risk and liability relating to loss, damage or injury to persons or property arising out of the presence of or use of the Products.

The relevant terms of the February 21, 2002 Contract are as follows:

> 8. **Warranty.** Product delivered hereunder will meet their manufacturer's standard specifications. Such specifications may be obtained by Purchaser upon request. Purchaser acknowledges that it may obtain devices which have the capability of testing whether the Products delivered hereunder meet such specifications. No claim of any kind with respect to any of the Products delivered hereunder, whether based on contract, negligence, warranty, strict liability or otherwise, shall be greater than the price paid for the Products in respect to which such claim is made. **THERE ARE NO EXPRESS WARRANTIES BY SELLER OTHER THAN THOSE SPECIFIED IN THIS PARAGRAPH 8. NO WARRANTIES BY SELLER (OTHER THAN WARRANTY OF TITLE AS PROVIDED IN THE UNIFORM COMMERCIAL CODE) SHALL BE IMPLIED OR OTHERWISE CREATED, INCLUDING BUT NOT LIMITED TO WARRANTY OF MERCHANTABILITY AND WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE UNDER THE UNIFORM COMMERCIAL CODE.**
>
> 9. **Liability.** Purchaser acknowledges that there are hazards associated with the use of the Products. It is Purchaser's responsibility to make its personnel concerned with the Products aware of such hazards and Purchaser undertakes and assumes all responsibility for warning its employees and independent contractors of all hazards to persons and property in any way connected with the Products. Purchaser also assumes all responsibility for the suitability and the results of using the Products. Purchaser assumes all risk and liability for loss, damages or injury to persons or property arising out of the presence of or use of the Products. Seller will not be liable for any special, indirect, incidental or consequential damages hereunder, whether arising from failure to deliver the Products or negligence, warranty, strict liability or otherwise.

These key limitation terms extinguish Federal's negligence, strict liability, and breach of warranty claims, and serve to limit any damage claims to an amount no greater than the price paid for the Products in respect to which such claim is made.

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III. LEGAL ARGUMENT

A. Legal Standard

Under the Federal Rules of Civil Procedure, summary judgment is proper only where "the pleadings, depositions, answers to interrogatories and admissions on file, together with affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." FED. R. CIV. P. 56(c). The moving party has the burden of demonstrating the absence of a genuine issue of fact before trial. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 256, 106 S. Ct. 2505, 2514, 91 L.Ed.2d 202 (1986). If the moving party satisfies the burden, the party opposing the motion must set forth specific facts showing that a genuine issue for trial remains. *Id.*; FED. R. CIV. P. 56(e).

Summary judgment is appropriate when the contract terms are clear and unambiguous, even if the parties disagree as to their meaning. *U.S. v. King Features Entertainment, Inc.*, 843 F.2d 394, 398 (9th Cir. 1988); *Int'l Union of Bricklayers v. Martin Jaska, Inc.*, 752 F.2d 1401, 1406 (9th Cir. 1985). Interpretation of a contract is a matter of law, including whether the contract is ambiguous. *Beck Park Apts. v. United States Dept. of Housing*, 695 F.2d 366, 369 (9th Cir. 1982); *Kassbaum v. Steppenwolf Productions, Inc.*, 236 F.3d 487 (9th Cir. 2000); *Kitty-Anne Music Co. v. Swan*, 112 Cal. App. 4th 30 (2003). Contract interpretation is essentially a judicial function to be exercised according to the generally accepted canons of interpretation so that the purposes of the instrument may be given effect. *Id.* Thus, the sole issue to be decided by this motion for summary judgment – whether the contract between PDI and Exelixis precludes a negligence, strict liability, and breach of warranty action against PDI – is a question of law wholly appropriate for the Court to determine on summary judgment without consideration of whether there is an absence of a genuine issue of material fact regarding the circumstances surrounding the incident.

B. The Contract Between PDI and Exelixis Precludes Federal's Negligence, Strict Liability and Breach of Warranty Action.

1. Federal Is Subrogated to the Rights of Exelixis.

An insurer that fully reimburses its insured is subrogated to the insured's rights and claims. *See Fireman's Fund Ins. Co. v. Wilshire Film Ventures*, 52 Cal. App. 4th 553, 555 (1997);

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Maryland Cas. Co. and National Amer. Ins. Co., 48 Cal. App. 4th 1822, 1829 (1996). A party entitled to subrogation has the same rights as an assignee of the claim. *Snider v. Basinger*, 61 Cal. App. 3d 819, 824 (1976). Thus, because Federal succeeds in subrogation to the rights of its insured, Exelixis, Federal's right to sue PDI for damages resulting from the alleged failure of the liquid nitrogen container under negligence, strict liability, and breach of warranty theories is governed and limited by the February 21, 2002 Contract between PDI and Exelixis.

2. The Clear and Unambiguous Terms of the Contract Explicitly Precludes Negligence, Strict Liability and Warranty Claims.

Under California law, the language of a contract is to govern its interpretation, if the language is clear and explicit. CAL. CIV. CODE § 1638. When a contract is reduced to writing, the intention of the parties is to be ascertained from the writing alone. CAL. CIV. CODE § 1639. The words of a contract are to be understood in their ordinary and popular sense, rather than according to their strict legal meaning; unless used by the parties in a technical sense, or unless a special meaning is given to them by usage, in which case the latter must be followed. CAL. CIV. CODE § 1644. A contract must receive such an interpretation as will make it lawful, operative, definite, reasonable, and capable of being carried into effect, if it can be done without violating the intention of the parties. CAL. CIV. CODE § 1643.

The clear and unambiguous terms of the February 21, 2002 Contract between PDI and Exelixis preclude Exelixis from asserting negligence, strict liability or warranty claims against PDI arising out of the presence of or use of the liquid nitrogen container. The February 21, 2002 Contract provides, *inter alia*: 1) "***No claim of any kind*** with respect to any of the Products delivered hereunder, ***whether based on contract, negligence, warranty, strict liability or otherwise***, shall be greater than the price paid for the Products in respect to which such claim is made..." and 2) "***Purchaser assumes all risk and liability for loss, damages or injury to persons or property*** arising out of the presence of or use of the Products. Seller will not be liable for any special, indirect, incidental or consequential damages hereunder, ***whether arising from failure to deliver the Products or negligence, warranty, strict liability or otherwise***." Under these terms, Exelixis was not entitled to bring an action for negligence, strict liability or breach of warranty arising out of

its use of the liquid nitrogen and the containers provided by PDI. As a result, Federal is also precluded from bring these same claims against PDI.

3. California Law Recognizes and Upholds Contractual Limitation of Liability Provisions Excluding Negligence, Strict Liability and Warranty Claims.

a. California Law Recognizes Contractual Limitation of Liability Provisions Exempting Negligence Where the Public Interest Is Not Involved.

California courts recognize and enforce contractual limitation of liability provisions such as those contained in the February 21, 2002 Contract. Section 1668 of the California Civil Code provides: "All contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against the policy of the law." While earlier California cases were in conflict regarding a party's ability to contractually exempt itself from negligence liability, the modern view is that a contract exempting liability for ordinary negligence is valid where no public interest is involved and no statute expressly prohibits it. *Gardner v. Downtown Porsche Audi*, 180 Cal. App. 3d 713, 716 (1986). Thus, California courts have generally upheld contractual liability exemptions for ordinary negligence where the public interest is not involved.[2]

[2] The California Supreme Court in *Tunkl v. Regents of University of California*, 60 Cal. 2d 92, 96 (1963) held that exculpatory provisions that "involve the public interest are unenforceable" and articulated six characteristics which have been held to stamp a contract as one affected with a public interest: (1) it concerns a business of a type generally thought suitable for public regulation; (2) the party seeking exculpation is engaged in performing service of great importance to the public, which is often a matter of practical necessity for some members of the public; (3) the party holds himself out as willing to perform this service for any member of the public who seeks it, or at least for any member coming within certain established standards; (4) as a result of the essential nature of the service, in the economic setting of the transaction, the party invoking exculpation possess a decisive advantage of bargaining strength against any member of the public who seeks his services; (5) in exercising a superior bargaining power the party confronts the public with a standardized adhesion contract of exculpation, and makes no provision whereby a purchase may pay additional reasonable fees and obtain protection against negligence; (6) as a result of the transaction, the person or property of the purchaser is placed under the control of the seller, subject to the risk of carelessness by the seller or his agents." Even a cursory analysis of the *Tunkl* factors clearly demonstrates that the contract between PDI and Exelixis is not one which involves the public interest. The February 21, 2002 Contract is a purely private business transaction and does not involve a transaction or involve any parties that have any bearing on the public interest.

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As one court explained, "[t]he general rule in California and other states is that exculpatory or indemnity clauses which attempt to free an actor from liability for his own negligence are basically valid but must be strictly construed and that failure to state an attempted exculpation or indemnity in plain, unambiguous and clear terminology will result in an interpretation that the clause was not intended to exempt the actor from liability for his own negligence. Notwithstanding this rule of strict interpretation, the contract must be interpreted by the court and the intent of the parties determined." *Delta Air Lines v. Douglas Aircraft Co.*, 238 Cal. App. 2d 95, 100 (1965).

That California law recognizes and enforces contractual limitations clauses is demonstrated by several cases. For example, in *Delta Air Lines v. Douglas Aircraft Co.*, 238 Cal. App. 2d 95, 100 (1965), plaintiff bought an airplane from defendant manufacturer for $2,250,000. A defective nose wheel caused the plane to veer off a runway, with resulting property damages of $233,881.35. The contract of sale contained a clause under which plaintiff buyer waived all "liabilities, express or implied, arising by law or otherwise and whether or not occasioned by Seller's negligence." The court held that the limitation provision was valid and relieved defendant of liability for the damages suffered by plaintiff as the clause clearly covered not only warranty but also tort liability for negligence. *Id.* The court specifically found that exemption from liability for negligence is permissible where the public interest is not involved, as is the case here involving a purely private business transaction. *Id.* at 104. As the court explained, "all that is herein involved is the question of which of two equal bargainers should bear the risk of economic loss if the product sold proved to be defective." *Id.*

In *Philippine Airlines, Inc. v. McDonnell Douglas Corp.*, 189 Cal. App.3d 234 (1987), a limitation of liability clause in a contract between an aircraft manufacturer and an airline for sale of an aircraft was held by the trial court to bar subsequent claims by the buyer for indemnity from the manufacturer in a personal injury action instituted against the airline by passengers who were injured during an aborted takeoff. The contract for sale had warranted the aircraft against defects, but limited buyer's remedies for breach to repair, replacement, or correction of any defective parts. The court affirmed the holding that the limitation of liability clause was a valid waiver of all rights by the airline to seek indemnity for payments made to personal injury claimants since it explicitly

stated the buyer waived all liability of the seller arising from negligence or with respect to consequential damages. *See also Continental Airlines, Inc. v. Goodyear Tire & Rubber Co.*, 819 F.2d 1519 (9th Cir. 1987) (finding exculpatory clause barring negligence and strict liability claims against aircraft manufacturer enforceable under California law).

As in the *Delta Air Lines* and *Philippine Airlines* cases, PDI's supply of gas products to Exelixis is a purely private business transaction between equal bargaining parties in a commercial setting and has no bearing whatsoever on the public interest. Thus, because California law recognizes and upholds limitation of liability provisions exempting negligence claims where the public interest is not involved, the Court should enter summary judgment against Federal and in favor of PDI on plaintiff's negligence claim.

b. California Law Recognizes Contractual Limitation of Liability Provisions Exempting Strict Liability Claims in the Commercial Setting.

In addition to barring negligence claims, California law allows contractual limitation of liability provisions to also bar strict liability claims. In *Appalachian Ins. Co. v. McDonnell Douglas Corp.*, 214 Cal. App. 3d 1 (1989), the court extended the validity of liability limitation clauses to include strict liability claims in the commercial context. In that case, a telecommunications satellite owned by plaintiff's insured failed to reach the desired orbit after being launched by an upper stage rocket manufactured and sold by defendant. Plaintiff's insurers had paid the insured their share of losses, and filed an action for negligence and strict products liability against defendant. Plaintiff argued that the limitation of liability clauses were unenforceable to the extent they attempt to bar claims for strict liability, arguing that strict liability claims cannot be contractually disclaimed. However, the court held that the doctrine of strict liability was not applicable in a commercial setting. While recognizing that there are cases which have held that strict liability cannot be contractually disclaimed in the consumer context, the court explained that "the doctrine of manufacturers' and suppliers' strict liability in tort was developed primarily to *protect individual consumers*." *Id.* (emphasis in original). In contrast, when lawsuits over a defective product arise in a commercial setting and involve only a business loss, courts have consistently held that the strict liability theory is not available and the parties are limited to normal commercial remedies under

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either the California Uniform Commercial Code or their contracts. As the court articulated, "strict liability theory should not apply to a commercial transaction because commercial entities are not 'in such vulnerable positions' as are consumers." *Id.* Therefore, the court found that liability for defects may be disclaimed since the tort theory of liability does not apply in this context and thus does not bar the disclaimer.

Similarly, in *Delta Air Lines, Inc. v. McDonnell Douglas Corp.*, 503 F.2d 239 (5th Cir. 1974), the Fifth Circuit, in interpreting California law, held that Section 1668 of the California Civil Code (the California statute declaring public policy against contracts to exempt anyone from responsibility for a law violation) did not invalidate an exculpatory clause relieving the seller of "all other warranties, guarantees, or liabilities, express or implied arising by law or otherwise and whether or not occasioned by seller's negligence." The Court specifically found that such a clause could be relied on in defense of civil actions counts for negligence, and that the clause was even broad enough to encompass strict liability in tort.

Under *Appalachian Ins. Co.*, Exelixis was not entitled (and thus Federal is not now entitled) to maintain a suit for strict liability against PDI for the alleged defect in the liquid nitrogen container supplied by PDI. The loss suffered by Exelixis and paid for by Federal under their insurance contract was solely a business loss that arose in a commercial setting and did not involve any claims of personal injury. In such a context, strict liability theory is simply not available and the parties are limited to commercial and contractual remedies. Because the February 21, 2002 Contract also explicitly precludes any strict liability claims arising from Exelixis' use of the PDI's products, the Court should enter summary judgment against Federal and in favor of PDI on plaintiff's strict liability claim.[3]

[3] To the extent plaintiff's are seeking purely economic losses without any personal or physical injuries, those damages are clearly barred by the economic loss rule. *See Seely v. White Motor Co.*, 63 Cal. 2d 9 (1965).

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c. The Warranty Disclaimer Contained in the February 21, 2002 Contract Are Enforceable Because The Provision Is Not Unconscionable.

With respect to Federal's breach of warranty claim, the contract between Exelixis and PDI contains a broad warranty disclaimer under the "Warranty" heading and providing: "**THERE ARE NO EXPRESS WARRANTIES BY SELLER OTHER THAN THOSE SPECIFIED IN THIS PARAGRAPH 8. NO WARRANTIES BY SELLER (OTHER THAN WARRANTY OF TITLE AS PROVIDED IN THE UNIFORM COMMERCIAL CODE) SHALL BE IMPLIED OR OTHERWISE CREATED, INCLUDING BUT NOT LIMITED TO WARRANTY OF MERCHANTABILITY AND WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE UNDER THE UNIFORM COMMERCIAL CODE.**" Warranty disclaimers are governed by Section 2-316 of Uniform Commercial Code (codified as CAL. COM. CODE § 2316). Section 2-316(2) provides:

> Subject to subdivision (3), to exclude or modify the implied warranty of merchantability or any part of it the language must mention merchantability and in case of a writing must be conspicuous, and to exclude or modify any implied warranty of fitness the exclusion must be by a writing and conspicuous. Language to exclude all implied warranties of fitness is sufficient if it states, for example, that "There are no warranties which extend beyond the description on the face hereof."

Under California law, a valid disclaimer provision must be in clear and distinct language and prominently set forth in large, bold print in such position as to compel notice. *Dorman v. Int'l Harvester Co.*, 46 Cal. App. 3d 11 (1975). Thus, courts have found that a warranty disclaimer in a purchase agreement was "conspicuous" where the disclaimer was both bold faced and set off in contrasting type and was the only section in the agreement set off in large type. *Siemens Credit Corp. v. Newlands*, 905 F. Supp. 757 (N.D. Cal 1994); *see also Nunes Turfgrass, Inc. v. Vaughn-Jacklin Seed Co., Inc.*, 200 Cal. App. 3d 1518 (1988) (upholding a provision limiting a seed seller's liability for negligence to purchase price as being governed by UCC).

The warranty disclaimer in the contract between Exelixis and PDI meets the "conspicuous language" requirement of the UCC as it is both set out in bold face and set off in contrasting all-caps typeface, and it is the only section in the agreement set off in large type. Furthermore, it is set forth in a separate section under the "Warranty" heading. As such, neither Exelixis or Federal can

make a valid argument that the disclaimer was invalid as unconscionable. Because the warranty disclaimer in the February 21, 2002 Contract is both valid and enforceable, the Court should enter summary judgment against Federal and in favor of PDI on plaintiff's breach of warranty claim barring Federal's warranty claim. Alternatively, pursuant to the terms of that provision, the Court should limit any damages for breach of warranty to be no greater than the price paid for the Products in respect to which such claim is made.

d. The Limitation of Liability and Limitation of Damages Provisions Should Be Enforced Because It Is Comprehensible, Clear and Explicit, and Free of Ambiguity or Obscurity.

To be sufficient as an exculpatory provision against one's own negligence, the party seeking to rely thereon must select words or terms clearly and explicitly expressing that this was the intent of the parties. *Basin Oil Co. of Calif. v. Baash Ross Tool Co.*, 125 Cal. App. 2d 578, 594; *Salton Bay Marina, Inc. v. Imperial Irrigation Dist.*, 172 Cal. App. 3d 914 (1985). Any contract of release from negligence must be comprehensible, clear and explicit, free of ambiguity or obscurity, and tell the prospective releasor that it is releasing the other from liability, including negligence. *Madison v. Superior Court*, 203 Cal. App. 3d 589 (1988); *Westlye v. Look Sports, Inc.*, 17 Cal. App. 4th 1715 (1993). Here, the contractual limitation of liability and limitation of damages provisions are clear, comprehensible, and free from ambiguity or obscurity. The provisions explicitly release any negligence, strict liability or breach of warranty claims against PDI. As a result, the Court should enforce these provisions set forth in the February 21, 2002 Contract and enter judgment against plaintiff Federal and in favor of defendant PDI as a matter of law.

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IV. CONCLUSION

Under California law, the limitation of liability and limitation of damages provisions contained in PDI's contract with Exelixis explicitly bars the plaintiff's breach of warranty, negligence, and strict liability claims. As a result, PDI respectfully requests that the Court grant PDI's motion for summary judgment and enter judgment in PDI's favor as a matter of law. Alternatively, PDI respectfully requests that the Court grant partial summary judgment in favor of PDI on those claim for which PDI must prevail as a matter of law.

Dated: July 29, 2005

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/s/

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